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## China - Peoples Republic of

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### South China 2013 Retail Annual Report

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Retail Foods

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**Report Highlights:**

In 2012, the economic outlook has gradually shifted away from the export-oriented model and toward domestic consumption and this is especially true in South China. The retail food sector kept growing but faced a number of new challenges. Penetration into secondary and third tier cities made the competition fiercer. Urbanization (in particular in rural areas) as well as infrastructure upgrades has fueled the consumption market. The total population of five South China provinces (Guangdong, Hunan, Fujian, Guangxi, and Hainan) reached 270 million, accounts to over one fifth of China's total population. In 2012, Guangdong's per capita GDP surpasses \$8,500 (RMB 54,095), a 7-percent increase compared to the previous year. Both the size of the middle class and overall income levels have increased. The per capita GDP of Guangzhou, for example, hit \$17,138 (RMB 109,000) and is leading the region's average by two percent which is now higher than Beijing and Shanghai. Massive infrastructure and industrial investment projects have driven the region's economic growth. In recent years, Hunan Province committed \$12 billion (RMB 75 billion) in investments projects targeting railways, highways, waterways and other transportation infrastructure. During the economic slowdown, Fujian was seeking new growth opportunities by emphasizing fisheries processing products in the national retail sector.

## General Information:

**Regional Retail Food Market Developments Overview:** The retail food sector has encountered a critical period of transition. The rapid expansion in the past five years in large cities has created an environment of intense competition. Retailers are actively identifying market development opportunities in second and third tier cities. New stores are more likely to be constructed in these cities than in first tier cities. In addition, new challenges from the on-line business sales channels and high operational and rental fees in first tier cities have forced both international and local retail chains to adjust and rethink their strategic expansion plans in Mainland China. Mergers and consolidation have enabled the leading players to capture greater market share away from smaller players. For some retailers this means transitioning from a volume-based approach to a value-focused approach will be need to drive sales. Similarly expansion speeds of many of the top retail chains slowed down as they upgrade key outlet stores' image.

Meanwhile, many retailers have had to close some outlets with poor sales performance. When developing expansion plans, retailers are more cautious than they were three years ago in selecting an ideal location to open a new retail outlet. There is greater specialization and consideration to the geographic location of an outlet that is being tied to customers they intend to reach. These branding and merchandizing strategies present opportunities for traders to take a more targeted approach in stimulating sales by hiring in-store promoters and working with individual outlets rather than dealing with a centralized procurement office. New value added services and existing store upgrades have become more important to retailers as they strive to differentiate themselves from competitors and establish their place in the market. Demand for imported food and beverage items has been on the rise as a result of increasing middle class consumers who are paying greater attention to food safety issues and aspire to a higher quality lifestyle. With the purpose of ensuring quality and reducing operation costs, direct farm purchasing and an integration of supply chain development practices have been strengthened by many retailers.

### New trends in China's retail sector

- a. The hypermarket format is being readjusted due to fierce competition and higher operational costs. Overseas retail chains (such as *Wal-Mart*, *Carrefour*, and *Tesco*) are striving to rise above the competition and survive the increasing rental fees incurred in first/secondary cities. Many retailers have opted to compete in third tier city markets and reduce property investment projects in large cities altogether. Around eight *Lotus* stores were also reported to close this year due to unbalanced profit/loss ratios. Meanwhile, *Carrefour* and *Tesco* are striving to survive in China with several negative reports about poor customer service, store closures and top management personnel changes.
- b. The next five-years are considered the golden age for Mainland China's e-commerce vendors. Not only has the giant ecommerce platform such as *TMall* and *Taobao* emerged as the largest leader in the retail sector, but also supermarket chain retailers have joined the pack to gain the new market share. *Yihaodian* (online retailer) with *Wal-Mart's* investment is one of these examples. According to sources in the trade, business with *Yihaodian* has been growing quickly.

- c. Other retail formats such as convenience stores and community stores also continue growing. Specialized food stores and fancy food outlets are picking up in secondary city markets, targeting affluent consumers who are not as price-sensitive and are looking for higher-end products.
- d. Wholesalers and retailers pay close attention to supply chain development –cold management is a prominent discussion topic. Although *Yihaodian* mainly targeted packaged foods in the past, this year, news reports revealed that although cold fresh delivery is a major challenge, *Yihaodian* expects higher sales revenues with the recent addition of fresh fruit delivery services launched in Shanghai (still on a trial basis). After the trial, *Yihaodian* will expand this service to South and North in the coming months.
- e. Demand for high quality imported food items is growing since consumers are more concerned about food safety. With increasing disposable income and dietary changes in the direction of healthier lifestyles, middle class consumers are willing to pay higher prices for imported food items. Imported milk formula and U.S. cherries, for example, are some premium products selling in most retail stores.
- f. Brands and packaging have become the new marketing strategies many have used to increase sales; such as gift packaging and packaging for designed to attract children are considered to be useful promotional tools. Gift-packing used to be a marketing tool for packaged items with longer shelf life, but recently there is a tendency that consumers favor fresh fruit in a gift packaging as well.
- g. Holiday promotions, especially *Chinese New Year* (generally in January or February) is optimal for good sales performances. Other holidays such as *Lantern Festival* (generally in September) and *Golden Week Holidays* are also considered as good seasons to increase sales. Food is one of the most important parts of local consumers' celebrations.
- h. Themed promotions, for example, the U.S. Fresh Fruit Festival or American Food Festival reached to secondary/ third tier cities. In Changsha, for example, the ten-day U.S. Northwest Cherry promotion under a theme of "The season of Love" received a positive sales feedback from local consumers.
- i. Products with greatest prospects: In South China, imported products with the greatest prospects include: snack food, dried fruits, 100% natural juice, wine, baby formula, fluid milk, candies, coffee, crackers, nuts, cheese, butter, yogurt, meat, food supplements and fresh fruits. In addition, cherries, blueberries, and cranberries are becoming popular since consumers are paying more attention to the nutritional benefits of these products.

### **Key Retailer profile**

**Wal-Mart (China):** Currently with over 380 stores nationwide, operating under various formats including supercenters (hyper market format), Sam's Club (membership retailer), and Trust Mart (smaller store format). In 2012, Wal-Mart faced several management challenges such as frequent top management personnel changes and an expansion slow-down. Although Wal-Mart opened around 30 new stores, this is relatively slow pace when compared with previous 40 plus new store which opened in 2011. This was due in part to having to close down several stores with lower profit margins due to poor sales performances. For

example, in Shenzhen, three “smart-choice” (community store format) outlets and one of the first supercenters opened in China were all closed in 2012. The Wal-Mart “Everyday Low Price” strategy seems to be challenged by innovation and value-added services. Demand for quality food and new varieties are growing. According to industry insiders, there are plans to close down over 100 Wal-Mart outlets that are underperforming by 2015, although Wal-Mart claims the chain will open 30 new outlets and upgrade another 50 outlets this year. According to some traders who have been in business with Wal-Mart, imported fresh fruit, for example, will be strengthened in *Wal-Mart* superstores to attract ongoing customers.

***Sam’s Club:*** In addition to *Wal-Mart* supercenters, *Sam’s Club* (membership warehouse stores) is another *Wal-Mart* format targeting middle class families and small businesses. *Sam’s Club* has an entirely independent and separate purchasing division and operation section than *Wal-Mart*. Selected brands in larger packages have made *Sam’s Club* a unique place to find family-size imported foods. The average per ticket sale in *Sam’s Club* is much higher (on average around 30 percent higher) than that of conventional supermarket competitors. For many local distributors, placing their products in *Sam’s Club* shelves brings their products higher status and credibility in the trade, because purchasing teams are quite particular about the performance of an SKU. To date, there are seven *Sam’s Clubs* outlets in Mainland China, including two in Shenzhen, one each in Beijing, Fuzhou, Dalian, Guangzhou and Shanghai. Two new *Sam’s Clubs* are set to open in Hangzhou and Suzhou. And it will compete with Metro for market share to source to small local restaurants (with no centralized purchasing departments). With more new outlets opening in China, *Sam’s Club* has begun direct sourcing for certain products from overseas. Products with prospect include seasonal fresh fruits and snacks.

***CR-Vanguard:*** By the end of 2012, there are a total of 4,425 outlets under *CR-V*’s brand. Last year alone, 782 outlets were opened, including 82 hypermarkets with sales floor space of (8,000-15,000 square meters). The merger of Jiangxi *Hongkelong* chain last year helped *CR-V*’s penetration into central inland cities.

***Olé/ BLT:*** Under the umbrella of *CRV Corporation*, *Olé* and *BLT* targets upper-middle income shoppers and white-collar workers. These supermarkets are usually located inside fancy shopping malls. The stores have been successful at introducing a wide assortment of imported food items such as cheeses, chocolates, coffee, wine, liquor, biscuits, and fresh fruits albeit at higher prices. Four years ago, the *Olé* brand encountered major problem due to an unstable supply chain and lack of promotion to support consumer demand; however, *Olé* does not seem to have that problem anymore and is planning to open more outlet in 1<sup>st</sup> and 2<sup>nd</sup> tier cities the near future. (ATO offices in China carried out a national promotion with this chain in 2012, for further information; please refer to GAIN report CH1858)

***AEON:*** The Japanese retail giant has a total of 102 various format outlets in China, previously known as Jusco. So far, in China there are four separate regional offices including: Shenzhen, Guangzhou, Qingdao, and Beijing. Each has separate and independent purchasing divisions. In March 2013, all stores were renamed *AEON* as part of the chain’s new strategy. It is expected that the re-organization of renamed *AEON group* will bring a brand new image to its consumers-- offering better service and a standardized procedure to its suppliers. *AEON* enjoys a favorable reputation in promoting imported food items, mainly from Japan, Korea and other countries. However, according to traders, the image of *AEON/Jusco* in the past two years has been downgraded from what it was in years past.

#### **Other formats:**

- **Pagoda:** is a leading specialized fresh fruit community chain store with the head office in Shenzhen. *It has over 400 outlets in Guangdong and Hainan provinces. It started about a decade ago with a franchise strategy. Pagoda mainly targets residential communities and families. Recently Pagoda established a branch office in Canada to support purchases of North American fresh fruit.*
- **7-Eleven** is a 24hour business model that made 7- Eleven a pioneer in Guangdong's convenience store sector. It has over 600 outlets concentrated in six cities including Guangzhou, Shenzhen and neighboring cities in the Pearl River Delta like Foshan, Dongguan, Zhongshan and Zhuhai. The chain targets young and office white collar customers. To attract more traffic, 7-Eleven has added services such as cell phone battery recharging stations, subway card sales, express delivery, fax, game card and tickets purchasing to attract greater traffic. Recently, 7-Eleven opened the door to franchising. With small sales floor (only 200 to 300 square meter), small packaged imported chocolates, candies, and biscuits are often available in store. It is also noted that some stores have displayed imported drinks and wine for sales. These products were supplied by various distributors.
- **Corners' Deli** is one of the fast growing specialized imported food stores. It has over 11 outlets in Guangdong and Hainan, all featuring a wide range of imported food items. With focus in Guangdong and Hainan, more single imported food shops were opened.
- **Watson's** is also expanding rapidly with over 300 stores offering selected imported food items. The purchasing office in Hong Kong is in charge of imported merchandise assortment selection.

